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CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Alex Sanchez

SUBJECT: SEE BELOW

DATE: March 27, 2001

Approved Date 03 · 27 · 01

INFORMATION

SUBJECT: DISTRIBUTION OF AFFORDABLE HOUSING FUNDS BY INCOME LEVEL

INTRODUCTION

During the past year, affordable housing advocates have suggested that the City modify its policy on the allocation of affordable housing funds between the various levels of qualifying incomes to put greater emphasis on extremely low-income households. On February 6, 2001, the City Council requested that an Information Memo be prepared to show the impact of changing the City's Income Allocation Policy to require that 60% of affordable housing funds be evenly divided between the very low-income and extremely low-income categories. This report provides the requested information.

BACKGROUND

In the adoption of the Mayor's Housing Task Force Report in 1988, the City Council for the first time adopted a policy on how affordable housing funds should be distributed among the various income categories eligible for assistance. The 1988 policy directed 60% of affordable housing funds to assisting very low-income (VLI) households, 25% to assist low-income (LI) households, and 15% to assist moderate-income (MOD) households.

In the adoption of the Five-Year Housing Investment Plan in 1995, the City Council modified the income allocation policy to say that the 60% directed to VLI households was a minimum, while the 25% and 15% directed to LI and MOD households were maximums. In other words, spending more that 60% on the VLI category and spending less than the 25% and/or 15% on LI and MOD is consistent with the policy.

ANALYSIS

Expenditure Patterns Since July 1999

The Housing Department is currently operating according to the Five-Year Spending and Operations Plan (FYSOP) adopted by the City Council in October 1999. The starting date for the FYSOP was July 1, 1999, which was also when the Housing Department began implementing the City Council's direction from earlier in 1999 to spend the 20% Supplement Funds from the Redevelopment Agency on housing affordable to extremely low-income (ELI) households.

The attached chart shows how affordable housing funds have been distributed among the various income categories based on funding decisions. That is, for new construction and acquisition/rehabilitation activities, the data represents the initial commitment by the City Council to fund a project. This is consistent with the way that data is being reported for the income-distribution performance measure in the City's Operating Budget.

The Council's policy on distribution of funds by income category applies to the totality of all programs administered by the Housing Department, with the exception of services to the homeless. Since July 1, 1999, the City Council and the Director of Housing have made funding commitments by the following distribution between income categories:

Extremely Low-Income	$ 25,493,468	24%
Very Low-Income	$ 53,692,819	50%
Low-Income	$ 16,441,535	15%
Moderate-Income	$ 11,666,137	11%
TOTAL	$107,293,959	

Proposal to Evenly Divide 60% of Funds Between ELI and VLI Categories

Affordable housing advocates have been pressing for a revision to the income-allocation policy that would evenly divide 60% of affordable housing funds between the ELI and VLI categories. While there is merit to the advocates' arguments that households at 30% or less of median income are paying a disproportionate share of their incomes on housing, there are policy and practical implications that the City Council would need to take into consideration should it wish to move forward with the proposal.

Before outlining those concerns, it needs to be noted how the existing ELI resources are being spent. The Redevelopment 20% Supplement funds being used to finance ELI units must be disbursed in the form of grants, not loans (a requirement for the use of tax-exempt bond proceeds). With a few exceptions, these funds and the 20%/HOME funds spent to date to subsidize units affordable to ELI households has been made in the form of grants for a small proportion of the units in any one project. The Department took this approach – on the advice of affordable housing developers – because ELI rents are barely able to cover operating and maintenance costs, leaving no additional rent revenue to service debt. Additionally, because it would be inequitable to burden the other 85-90% of the units in a development with making debt-service payments on behalf of the ELI units, the grants for ELI units have been roughly twice the amount, on a per-unit basis, as the City's loan amount for VLI or LI units.

The policy and practical implications of the proposed income-allocation policy revision include:

- **Pipeline Projects**. Numerous affordable housing developments are in the pre-zoning and pre-funding commitment phase of the process. The sponsors of those developments already have determined what income mix is going to make a specific project work at a specific location, subject to the design and improvement requirements of that location, and taking into account the cost of acquiring that site. While it will be possible for the Housing Department to convince many of these developers to make 10-15% of the units in these projects affordable to ELI households, as the Department has done over the past 20 months, it is not probable that any higher percentage – which would be needed to balance the expenditures for ELI and VLI – will be financially feasible.

- **Investor Resistance**. While the affordable housing developers we work with have been cooperative in trying to implement the Council's direction to produce ELI units with the Redevelopment 20% Supplement funds, they have encountered resistance in some instance from tax-credit investors to individual projects receiving grant funds. The value of the tax-credit investment is enhanced by the amount of debt that the project will carry, and some investors have threatened to reduce the amount of tax-credit equity that they would be willing to put into projects. Most affordable housing projects in San Jose have either 9% or 4% tax credits as part of their financing structures. The effect on the pipeline projects noted above would be exacerbated if not all developments seeking City funding will be accepting their fair share of the grant-funded ELI units.

- **Effect on Production**. The 1999-04 Spending and Operations Plan adopted by the City Council in October 1999 calls for the completion of 6,036 new affordable housing units. Approximately 55% of these units are far enough along in the predevelopment or development process (or have been completed) to be unaffected by the proposed policy change. However, assuming that the proposed policy change were to be implemented today and also assuming a constant volume of affordable housing resources being available, there would be a 350-unit shortfall (or about 6%) in meeting the 6,036-unit target.

It should also be noted in this context that the Mayor has proposed that an additional $10 million be budgeted for the 20% Supplement in the Redevelopment Agency's upcoming five-year capital improvement program, bringing the total in that program to $34.5 million since 1998. Furthermore, starting in July 2001, the Redevelopment Agency will begin reimbursing the Housing Department for units produced to satisfy the Agency's Downtown and Hellyer/Piercy replacement housing obligations. Since this money – conservatively estimated at $8 million over the next few years – will be in the form of tax-exempt bond proceeds and must be granted (i.e., cannot be loaned), the Housing Department will be using the replacement housing funding to finance ELI units. However, expenditure of these funds from the Redevelopment Agency will not appreciably affect the division of resources between units affordable at the ELI and VLI levels since it will only sustain a continuation of the current 24%/50% split experienced since 1999.

CONCLUSIONS

Allocation of affordable housing funds by income categories in the first 19 months of the Five-Year Spending and Operations Plan is consistent with adopted City Council policy. Because of the policy and practical implications cited above, the Housing Department has reservations about revising the income-allocation policy to evenly divide 60% of affordable housing resources between the extremely low- and very low-income categories.

ALEX SANCHEZ
Director of Housing

Attachment

c: Housing Advisory Commission

Attachment

Affordable Housing Program

DISTRIBUTION OF FUNDS BY INCOME CATEGORY

July 1, 1999 thru February 15, 2001

Program	Extremely Low-Income 30% of Median Income	Very Low-Income 50% of Median Income	Low-Income 65% of Median Income*	Moderate-Income 120% of Median Income*
New Construction	$22,764,886	$50,320,343	$10,817,146	$3,901,340
%-age Breakdown	26%	57%	12%	4%
Acquisition/ Rehabilitation	$0	$1,106,322	$4,393,678	$0
%-age Breakdown		20%	80%	
Rehabilitation & Paint Program	$2,728,582	$2,266,154	$1,230,711	$764,797
%-age Breakdown	39%	32%	18%	11%
Homebuyer Programs	$0	$0	$0	$7,000,000
%-age Breakdown				100%
TOTAL	**$25,493,468**	**$53,692,819**	**$16,441,535**	**$11,666,137**
%-age Breakdown	24%	50%	15%	11%

* Low-income as a percentage of median income varies from year to year.

** The City Council's general policy is that moderate-income should be capped at 100% of median income. However, the Council has approved exceptions to that policy from time to time, and some of those exceptions are accounted for in this data.